

Congress of the United States  
CONGRESSIONAL OVERSIGHT PANEL

## Opening Statement of J. Mark McWatters

### Congressional Oversight Panel Field Hearing on Commercial Real Estate

Atlanta, Georgia  
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Thank you Professor Warren.

I very much appreciate the attendance of the distinguished witnesses that we have today. I look forward to hearing their views.

There is little doubt that much uncertainty exists within the present commercial real estate, or CRE, market. According to the Real Estate Roundtable<sup>1</sup>:

- i. CRE values have declined by approximately \$2 trillion since June 2008;
- ii. Approximately \$3.3 trillion of CRE debt remains outstanding;
- iii. Approximately \$300 billion of CRE debt matures annually, yet existing financial institutions cannot meet the refinancing demand;
- iv. Banks hold over \$500 billion of construction and land development loans and exposure is far higher for regional and community banks than for money center institutions;
- v. Banks and commercial mortgage-backed securities, or CMBS, provide approximately 80 percent of the CRE debt financing, yet both sources remain substantially shut down to new lending;
- vi. Distressed loans in special servicing are growing at a rate of \$2-3 billion per month; and
- vii. Broad based recognition of CRE related losses has yet to occur and significant problems are expected in 2010-2012.

In order to suggest a solution to the challenges currently facing the CRE market it is critical that we thoughtfully identify the sources of the underlying difficulties. Without a proper diagnosis it is likely that we may craft an inappropriately targeted remedy with adverse unintended consequences.

Broadly speaking, it appears that today's CRE industry is faced with both an oversupply of CRE facilities *and* an undersupply of prospective tenants and purchasers. In my view, there has been an unprecedented collapse in demand for CRE property and that many potential tenants and purchasers have withdrawn from the CRE market not simply because rental rates or purchase prices are too high but because their

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<sup>1</sup> See [www.rer.org](http://www.rer.org).

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business operations do not presently require additional CRE facilities. Over the past few years while CRE developers have constructed new office buildings, hotels, multi-family housing, retail and shopping centers and manufacturing and industrial parks, the end users of such facilities have suffered the worst economic downturn in several generations. Any posited solution to the CRE problem that focuses only on the oversupply of CRE facilities to the exclusion of the economic difficulties facing the end users of such facilities appears unlikely to succeed. The challenges confronting the CRE market are not unique to that industry, but, instead, are indicative of the systemic uncertainties manifest throughout the larger economy.

In order to address the oversupply of CRE facilities, developers and their creditors are currently struggling to restructure and refinance their portfolio loans. In some instances creditors are acknowledging economic reality and writing their loans down to market value with, perhaps, the retention of an equity participation right. In other cases lenders are merely “kicking the can down the road” by refinancing problematic credits on favorable terms at or near par so as to avoid the recognition of losses and the attendant reductions in regulatory capital. While each approach may offer assistance in specifically tailored instances, neither addresses the underlying economic reality of too few tenants and purchasers of CRE facilities.

Until small and large businesses regain the confidence to hire new employees and expand their business operations it is doubtful that the CRE market will sustain a meaningful recovery. As long as businesspersons are faced with the multiple challenges of rising taxes, increasing regulatory burdens, enhanced political risk associated with unpredictable governmental interventions in the private sector as well as uncertain health care and energy costs, it is unlikely that they will enthusiastically assume the entrepreneurial risk necessary for protracted economic expansion and a recovery of the CRE market. It is fundamental to acknowledge that the American economy grows one-job and one-consumer purchase at a time, and that the CRE market will recover one-lease, one-sale and one-financing at a time. With the ever expanding array of less than friendly rules, regulations and taxes facing businesspersons and consumers we should not be surprised if businesses remain reluctant to hire new employees, consumers remain cautious about spending, and the CRE market continues to struggle.

The problems presented by today’s CRE market would be far easier to address if they were solely based upon the mere oversupply of CRE facilities in certain well delineated markets. In such event, a combination of restructurings, refinancings and foreclosures would most likely address the underlying difficulties. Unfortunately, the CRE market must also assimilate a remarkable drop in demand from prospective tenants and purchasers of CRE properties who are suffering a reversal in their business operations and prospects.

In my view, the Administration could jump start the prompt and robust recovery of the CRE market--as well as the overall U.S. economy--by sending an unambiguous message to the private sector that it will not directly or indirectly raise the taxes or increase the regulatory burden of CRE market participants and other business enterprises. Without such express action, the recovery of the CRE market will most likely proceed at a sluggish and costly pace that may foreshadow the Secretary’s allocation of additional TARP funds to financial institutions that hold CRE loans and commercial mortgage-backed securities.

Thank you for joining us today and I look forward to our discussion.